

Message Text

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PAGE 01 MANILA 00852 161014Z

63

ACTION TRSE-00

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USADB

FOR NAC AGENCIES

PASS TREASURY FOR ZINMAN/MEYERS

E.O. 11652: ADS, DECLAS 7/16/76

TAGS: EAID, EFIN

SUBJECT: REVIEW OF BANK'S RESOURCE POSITION AND PROPOSAL FOR
INCREASE IN BANK'S CAPITAL STOCK

REF: (A) MANILA 1773, (B) TREASURY 75-222

1. ON JANUARY 14, BANK DISTRIBUTED WORKING PAPER 1-76
WHICH IS ONE OF THREE WORKING PAPERS PROPOSED FOR DISCUSSION
AT BOARD OF DIRECTORS' MEETINGS SCHEDULED FOR JANUARY 27
AND 29. OWRKING PAPER 1-76 WAS POUCHED JANUARY 15.

2. WORKING PAPER 1-76 CONTAINS BANK RESPONSE AND COMMENTS
ON SIX MAJOR ISSUES RAISED AT MEETING OF BOARD OF DIRECTORS
ON DECEMBER 16. THEY ARE:

(A) TIMING OF CAPITAL INCREASE. DISCUSSION CONSIDERED
METHODS TO POSTPONE THE PROPOSED CAPITAL INCREASE BEYOND
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PAGE 02 MANILA 00852 161014Z

MID-1977 TO MID-1978. QUESTIONS FOCUSED ON THE VALIDITY

OF AND THE REDUCTION IN THE 25 PERCENT SAFETY MARGIN OF CONVERTIBLE CALLABLE CAPITAL AND ON THE OVERLAP BETWEEN THE COMPLETION OF SUBSCRIPTIONS ON THE FIRST GENERAL CAPITAL INCREASE AND THE BEGINNING OF THE PROPOSED SECOND GENERAL CAPITAL INCREASE WHICH IS PRIMARILY A CONCERN OVER THE ABILITY OF THE U.S. TO COMPLETE THE FIRST CAPITAL INCREASE. THE BANK'S POSITION IS THAT THE SAFETY MARGIN IS NECESSARY TO IMPORVE THE BANK'S FINANCIAL POSITION IN CAPITAL MARKETS THAT WILL HOPEFULLY LEAD TO A REDUCTION IN BORROWING COSTS. ALSO THE BANK HOPES THAT THE U.S. WILL HAVE COMPLETED THE FIRST CAPITAL INCREASE BY MID-1977.

(B) LENDING RATE. DIRECTORS QUESTIONED THE USE OF THE CURRENT LENDING RATE AND COMMITMENT CHARGE IN THE PROJECTIONS PROVIDED IN APPENDIX 2 TO 4 IN ADB DOCUMENT R111-75. THE BANK'S POSITION IS THAT THE PROJECTIONS MUST BE BASED ON CURRENT PRACTICE SINCE CHANGES IN LENDING RATES AND/OR COMMITMENT CHARGES ARE POLICY ISSUES THAT REQUIRE DECISION BY THE BOARD OF DIRECTORS.

(C) DISBURSEMENT PROJECTIONS. DIRECTORS QUESTIONED USE OF THE RECENT EIGHT YEAR WORLD BANK DISBURSEMENT EXPERIENCE FOR ADB PROJECTIONS IN APPENDIX 1 OF ADB DOCUMENT R111-75. BANK EXPLAINED THAT WHILE BANK WILL COMPLETE ITS OWN DISBURSEMENT EXPERIENCE IN THE FUTURE, BANK DISBURSEMENT EXPERIENCE ON SIX INITIAL LOANS, WHILE INADEQUATE, IS SUGGESTIVE OF EIGHT YEARS.

(S) FINANCIAL INDICATORS. THIS SECTION FOCUSES ON ASPECTS OF THE RESERVE-LOAN RATIO AND NET INCOME. BANK EXPLAINS THAT NET INCOME PROJECTIONS ARE BASED ON THE NEED TO MAINTAIN INCOME AND RESERVES TO ENSURE INTEREST COVERAGE OF NOT LESS THAN 1.25 AND A RESERVE-LOAN RATION OF NOT LESS THAN 0.15 DURING THE FUNDING PERIOD OF THE PROPOSED GENERAL CAPITAL INCREASE. NET INCOME IS ESTIMATED BY THE SUM OF PROJECTIONS OF SIX ITEMS. THE BANK NOTES THAT THESE PROJECTIONS ARE EXPLAINED IN SECTION III AND IV OF DOCUMENT R111-75 AND THE ASSUMPTIONS ARE DETAILED IN APPENDIX 1.

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PAGE 03 MANILA 00852 161014Z

3. ON RESERVE-LOAN RATIO OF NOT LESS THAN 15 PERCENT, RESERVES INCLUDE SPECIAL RESERVES AND LOAN IS DEFINED AS THE NET LOAN AMOUNT DISBURSED AND OUTSTANDING. BANK EXPLAINS THAT ADB CONCEPT DIFFERS FROM THAT USED BY WORLD BANK AS DESCRIBED IN PARA. 37 OF DOCUMENT R111-75. IF ADB FORMULA IS USED ON WORLD BANK DATA, PERCENTAGE DECLINES FROM 34.6 PERCENT IN 1972 TO 25.4 PERCENT IN 1975 AND PROJECTED TO DECLINE TO 16.3 PERCENT IN 1980

AND 11.2 PERCENT. BANK STAFF AGREES THAT ADB SHOULD BEGIN TO FORMULATE ITS OWN POLICIES OF FINANCIAL INDICATORS INCLUDING ADEQUATE RESERVES.

4. IF THE WORLD BANK FORMULA WERE USED ON ADB PROJECTIONS ADB RESERVE-LOAN RATION IN 1981 WOULD BE 0.23 IN APPENDIX 3 AND 0.29 IN APPENDIX 4.

(E) USE OF PAID-IN INCONVERTIBLE CURRENCIES FOR ADMINISTRATIVE EXPENSES. BANK EXPLAINS THAT ARTICLE 24.5 ENVISAGES NO RESTRICTION ON USE OF THESE CURRENCIES FOR ADMINISTRATIVE EXPENSES. HOWEVER, IN PRACTICE, THERE ARE CERTAIN RESTRICTIONS. FOR TRAVEL EXPENSES, CHECKS CAN BE DRAWN ON LOCAL CURRENCY ACCOUNTS AT CENTRAL BANKS IF A VISIT OF STAFF MEMBER EXCEEDS THREE BUSINESS DAYS AND THEN ONLY 50 PERCENT OF PER DIEM AND 100 PERCENT OF INLAND TRANSPORTATION, COMMUNICATIONS AND REPRESENTATION ALLOWANCES ARE CLAIMED. IN ADDITION, THERE HAVE BEEN DIFFICULTIES IN CASHING CHECKS, PARTICULARLY IN CASES OF SHORT VISITS WHERE INLAND TRAVEL IS REQUIRED. BANK STATES THAT NEW ARRANGEMENTS WILL BE EXAMINED TO PERMIT PROMPT ENCASHMENT OF LOCAL CURRENCY CHECKS. ATTACHED TO THIS WORKING PAPER IS A TABLE INDICATING USE OF LOCAL CURRENCIES. FOOTNOTES TO TABLE REFER TO CURRENCIES REQUESTED AND USED UNDER APPROVED LOANS.

(F) GROWTH IN ADMINISTRATIVE EXPENSES. DIRECTORS QUESTIONED THE NEED FOR AN ANNUAL 17 PERCENT INCREASE IN ADMINISTRATIVE EXPENSES WHEN PERCENTAGE INCREASE IN PROJECTED LENDING DECREASES FROM 18.5 PERCENT IN 1976 TO 9.6 PERCENT IN 1981. THE BANK INDICATED THAT VOLUME OF LENDING IS ONLY ONE OF THE FACTORS IN GROWTH OF ADMINISTRATIVE EXPENSES. WORKING PAPER IDENTIFIES FIVE AREAS IN BANK OPERATIONS THAT REQUIRE EXPANSION AS THE LIMITED OFFICIAL USE

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PAGE 04 MANILA 00852 161014Z

VOLUME OF LENDING INCREASES. IN ADDITION, BANK STAFF NOTES THAT IN REAL TERMS, GROWTH WOULD AVERAGE ABOUT 7 PERCENT.

5. THE OTHER TWO WORKING PAPERS WILL BE (A) AN UPDATE OF SECTIONS I AND II OF WORKING PAPER 4-75 DATED 24 FEB. 1975 TO REVISE ESTIMATES OF AID REQUIREMENTS FOR REGIONAL DEVELOPING MEMBER COUNTRIES AND (B) PROJECTIONS OF PROPOSED SECOND GENERAL CAPITAL INCREASE BASED ON LOWER AND HIGHER CAPITAL INCREASES. OTHER PARAMETERS WILL BE VARIED TO PROVIDE A SENSITIVITY ANALYSIS THAT MAY BE USEFUL TO JUSTIFY A 15 PERCENT PAID-IN CAPITAL. STAFF EXPECTS TO DISTRIBUTE THESE TWO WORKING PAPERS IN A FEW DAYS.
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